IN THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF TENNESSEE

In re CRAIG ARTHUR THOMPSON and JILL ANN THOMPSON Debtors.	No. 01-20946 Chapter 7
GEORGE KUSHNER and wife, MADELINE KUSHNER, Plaintiffs, vs. CRAIG ARTHUR THOMPSON and wife, JILL ANN THOMPSON, and TRAVIS THOMPSON, Defendants.	Adv. Pro. No. 01-2053

M E M O R A N D U M

APPEARANCES:

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MARCIA PHILLIPS PARSONS
UNITED STATES BANKRUPTCY JUDGE

This adversary proceeding is before the court on defendant Travis Thompson's motion to dismiss or for summary judgment. For the reasons discussed below, the motion will be granted. This is a noncore, related proceeding to which the parties have implicitly consented to entry of final orders by this court.[1] See 28 U.S.C. § 157(c)(2).

I.

The underlying chapter 7 bankruptcy case was commenced by the debtors Craig and Jill Thompson on March 19, 2001. Plaintiffs George and Madeline Kushner filed their complaint initiating this action against the debtors on September 13, 2001, seeking, *inter alia*, a nondischargeability determination pursuant to 11 U.S.C. § 523(a)(2), (4) or (6). The basis for the lawsuit is an agreement dated June 1, 1997, a copy of which is attached to the complaint, whereby the debtors agreed to purchase from the plaintiffs the shares of Lord George of Tri-Cities, Inc., a Tennessee corporation, for $80,000. The

[1]Although in his answer Travis Thompson "asserts this court lacks jurisdiction over defendant in bankruptcy to adjudicate non bankruptcy core issues without consent of the parties," the court finds the parties have consented to entry of an order on the present motion: Travis Thompson by moving the court for relief on his pending motion and the plaintiffs by having joined Travis Thompson as an additional defendant in what would otherwise be strictly a core proceeding.

agreement provided for $20,000 of the purchase price to be paid at closing with the remaining balance of $60,000, along with an existing indebtedness of $48,000 owed by the debtors to the plaintiffs, to be paid in installments over a ten-year period at 9%. A promissory note to this effect was made by the debtors and secured by a blanket security interest from the corporation. Plaintiffs aver in their complaint that the debtors defaulted on the note and agreement prior to the bankruptcy filing and thereafter they "foreclosed upon ... and sold at public auction the equipment and inventory" of the corporation and "attached the [corporation's] bank account," leaving a balance owing by the debtors of $49,158.65.

For their cause of action, the plaintiffs contend that the debtors willfully impaired the plaintiffs' security interest by diverting cash from the corporation and payments for services performed on behalf of the corporation to their own personal use and by transferring corporate assets to their son, Travis Thompson. The plaintiffs also claim that the debtors failed to return certain motor vehicles covered by the security interest granted to the plaintiffs. Finally, the plaintiffs assert that the debtors:

> conspired with their son, Travis Thompson, to set up a competing corporation; that they transferred Corporate/ Guarantor assets and equipment to the competing corporation; that they transferred customers

> and business to the competing corporation; that they drained the assets of the Corporation/Guarantor; that they then filed for personal bankruptcy protection in an attempt to discharge the Kushners' debt and are at this time engaged in the same business as that of the Corporation/ Guarantor, i.e., selling and servicing fireplace and grilling systems.

In this regard, the plaintiffs aver that the debtors are in breach of a covenant contained in the agreement providing "that they would not engage in any similarly related business except though the Corporation." In addition to the nondischargeability determination, the plaintiffs request in their prayer for relief that the court (1) enter an order allowing them to join Travis Thompson as a defendant "so that he may be subject to this Court's jurisdiction"; (2) grant the plaintiffs a judgment against both the debtors and Travis Thompson for compensatory damages in the amount of $100,000 and $100,000 in punitive damages; and (3) determine the rights of the parties in the motor vehicles.

By agreed order entered December 18, 2001, the plaintiffs were permitted to amend their complaint to add Travis Thompson as a defendant. The plaintiffs' amended complaint which accompanied the proposed agreed order only contains allegations that Travis Thompson is the debtors' son and resides in Sullivan County, Tennessee. The plaintiffs did request in their amended complaint additional relief "[t]hat the court temporarily and

permanently ... enjoin the Defendants either individually, or by and through others, from engaging in the business of selling and servicing fireplace and grilling systems." Upon the plaintiffs' subsequent motion, the question of whether a preliminary injunction should issue was brought before the court at a March 5, 2001 hearing. The motion was denied as the court found that the plaintiffs could be fully compensated by money damages and therefore the plaintiffs could not demonstrate irreparable harm, a necessary element for entry of an injunction.

Discovery has now been completed and trial is scheduled for November 14, 2002. The present motion was filed by Travis Thompson on September 30, 2002, along with a memorandum of law. Plaintiffs filed their memorandum in response on October 16, 2002. Although no affidavits were filed by the parties, both memoranda refer to portions of the transcripts from the parties' depositions as attached.

II.

Rule 56 of the Federal Rules of Civil Procedure, as incorporated by Fed. R. Bankr. P. 7056, mandates the entry of summary judgment "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with affidavits, if any, show that there is no genuine issue as to

any material fact and that the moving party is entitled to judgment as a matter of law." "When reviewing a motion for summary judgment, the evidence, all facts, and any inferences that may be drawn from the facts must be viewed in the light most favorable to the nonmoving party." *Poss v. Morris (In re Morris)*, 260 F.3d 654, 665 (6th Cir. 2001)(citing *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986)). To prevail, the nonmovant must show sufficient evidence to create a genuine issue of material fact and from which the court could reasonably find for the nonmovant. *Id.* (citing *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 252 (1986)). "Entry of summary judgment is appropriate 'against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden of proof at trial.'" *Id.* (quoting *Celotex Corp. v. Catrett*, 477 U.S. 317, 322, (1986)). In other words, a nonmoving party has the affirmative duty to direct the court's attention to specific portions of the record upon which it seeks to rely to create a genuine issue of material fact. *Id. See also Street v. J.C. Bradford & Co.*, 886 F.2d 1472 (6th Cir. 1989).

III.

The court will first address plaintiffs' claim for an injunction against the defendant Travis Thompson. In their memorandum, the plaintiffs state that "this case involves claims ... against the Debtors ... and their son, Travis Thompson to determine the dischargeability of debt of the Debtors and to enjoin all these Defendants from engaging in a conspiracy of selling and servicing fireplace and grilling systems in contravention of a written agreement by the Debtors not to do so." The plaintiffs go on to explain their theory in greater detail as follows:

> The Defendants in concert with their son, Travis Thompson, have transferred assets to Travis Thompson and are attempting to use confidential information and assets which rightfully belong to [the plaintiffs] to compete against them in direct violation of the Agreement to further damage the Kushners and deny them their property and contractual rights.

Indeed, the main tenet of the plaintiffs' lawsuit is based on their understanding that the plaintiffs are obligated under the agreement to refrain from engaging in any similar business in any fashion until the indebtedness is paid. However, that does not appear to be what the terms of the agreement provide.

The debtors, defined as "Purchaser" under the agreement, undertake several covenants, including one at subparagraph 7(i) which the plaintiffs allege the debtors have continued to

violate:

> Consolidation or Merger; Sale or Acquisition of Assets. Company will not enter into any transaction of merger or consolidation, acquire any other business or corporation, acquire all or substantially all of the property or assets of any other individual, partnership, corporation, trust, association or other form of organization, or sell, lease, transfer or dispose of all or a substantial part of its assets, without the prior written consent of Seller, which consent shall not be unreasonably withheld. ***Purchase[r] shall not engage in any similarly related business except though the Company.*** (Emphasis supplied.)

At subparagraph 3(b), which discusses what happens upon a default, the agreement states:

> Default. In the event the Purchaser defaults in the payment of the promissory note or the Purchaser or Company default on any other obligation to Seller, the Seller shall give written notice of such default to the Escrow Agent. The Escrow Agent shall thereupon, and with reasonable dispatch, sell for the account of the Purchaser all or any part of the shares held by the Escrow Agent, at public or private sale in such quantities or lots as shall seem best to the Escrow Agent in his absolute discretion. After first applying the proceeds of sale to the payment of the expenses of sale, the Escrow Agent shall then apply the proceeds to the satisfaction of the unpaid promissory note of the Purchaser, and thereafter apply the remaining proceeds to the payment of any obligation of Purchaser or Company to Seller and then pay any surplus and deliver any unsold shares to the Purchaser. ***Thereupon, all obligations between the Seller, Company and Purchaser and of the Escrow Agent shall cease, except that the Purchaser and Company shall be liable to the Seller for any deficiency if the sale or sales produce an amount insufficient to pay all the unpaid obligations of the Purchaser and Company.*** (Emphasis supplied.)

The plaintiffs allege that upon the debtors' default in payment of the note, they exercised their option to foreclose and are now pursuing the deficiency balance. As a result, the debtors' obligation under subparagraph 7(i) of the agreement "to not engage in any similarly related business except though the Company" ceased pursuant to subparagraph 3(b). Thus, there is no basis to enjoin the defendant Travis Thompson "from engaging in the business of selling and servicing fireplace and grilling systems" as the plaintiffs request in their amended complaint. Accordingly, the defendant is entitled to summary judgment in this regard.

The court turns next to the plaintiffs' claim for a monetary judgment against the defendant Travis Thompson. This issue is not as easily analyzed as the injunction issue because the precise nature of the plaintiffs' complaint against Mr. Thompson is somewhat unclear. As previously noted, the only specific allegations in the complaint regarding Travis Thompson is that the debtors conspired with him to set up a competing corporation and that the debtors, as officers of the corporation, transferred to their son Travis Thompson assets of the corporation in which the plaintiffs had a security interest. In his memorandum in support of his motion to dismiss or for summary judgment, Mr. Thompson asserts that he had neither a

contractual nor fiduciary duty to the plaintiffs, that the evidence does not establish conspiracy to induce the breach of the agreement between the debtors and the plaintiffs, and that any assets in which the plaintiffs had a security interest have been returned. In their responsive memorandum of law, the plaintiffs assert that they "are not suing Travis Thompson on a contract theory, but are instead suing Travis Thompson on a tort theory of a conspiracy to defraud" the plaintiffs based on Mr. Thompson's alleged fraudulent receipt of corporate assets. The plaintiffs also contend in their memorandum that Mr. Thompson participated in a conspiracy with the debtors, "the common purpose of which was to breach the Debtors' fiduciary duty to the Corporation."

In Tennessee, conspiracy to defraud "is defined as a 'combination between two or more persons to accomplish by concert an unlawful purpose, or to accomplish a purpose not in itself unlawful, but by unlawful means.'" *Brown v. Birman Managed Care, Inc.*, 42 S.W.3d 62, 67 (Tenn. 2001)(quoting *Dale v. Thomas H. Temple Co.*, 208 S.W.2d 344, 353 (Tenn. 1948)). "Each conspirator must have the intent to accomplish this common purpose, and each must know of the other's intent." *Id.*

In this regard, it must be emphasized that "[c]onspiracy, without proof of fraud, is not a cause of action." *USI*

Exchange, Inc. v. Long Pontiac Co., 1998 WL 881860, *6 (Tenn. App. Dec. 17, 1998). As recognized by the United States Supreme Court, "[t]here is no tort of civil conspiracy in and of itself [as] there must first be pleaded specific wrongful acts which might constitute an independent tort." *Beck v. Prupis*, 529 U.S. 494 (2000)(quoting *Satin v. Satin*, 69 A.D.2d 761, 762 (1979)). "The plaintiff must allege all the elements of a cause of action for the tort the same as would be required if there were no allegation of a conspiracy." *Id*. (quoting *J. & C. Ornamental Iron Co. v. Watkins*, 152 S.E.2d 613, 615 (Ga. App. 1966)).

In the Tennessee Supreme Court's most recent pronouncement of the elements required to establish common law fraud, the court stated:

> When a party intentionally misrepresents a material fact or produces a false impression in order to mislead another or to obtain an undue advantage over him, there is a positive fraud. The representation must have been made with knowledge of its falsity and with a fraudulent intent. The representation must have been to an existing fact which is material and the plaintiff must have reasonably relied upon that misrepresentation to his injury.

Birman Managed Care, Inc., 42 S.W.3d at 66-67.

Considering the allegations of the complaint and the amended complaint as a whole, the complaint fails to allege all of the required elements of fraud. There is no assertion that the

defendants "intentionally misrepresent[ed] a material fact or produce[d] a false impression in order to mislead ... or to obtain an undue advantage" over the plaintiffs. Similarly, there are no allegations in the complaint regarding knowledge of any alleged falsity, fraudulent intent, or reasonable reliance. In light of these absences and the requirement imposed by Fed. R. Civ. P. 9(b) that fraud must be pleaded with particularity, the complaint fails to state a claim for fraud. As such, it also fails to state a claim for conspiracy to defraud against defendant Travis Thompson. Accordingly, his motion to dismiss the complaint, to the extent it seeks damages against him for conspiracy to defraud, will be granted.

To the extent the complaint sets forth a claim against Travis Thompson for inducement to breach a contract, he is entitled to summary judgment. Under Tennessee law, there are seven elements to an action for inducement to breach a contract:

> The plaintiff must prove that there was a legal contract, that the wrongdoer had sufficient knowledge of the contract, and []he intended to induce its breach. Further, that the wrongdoer acted maliciously, and the contract was, in fact, breached, and the alleged act was the proximate cause of the breach, and damages resulted from that breach.

Baker v. Hooper, 50 S.W.3d 463, 468 (Tenn. App. 2001). Without regard to the other elements of the cause of action, there is no evidence that the defendant Travis Thompson had "sufficient

knowledge of the contract." Travis Thompson testified in his deposition that he had no knowledge of the terms in the agreement including any which restricted his parents from engaging in a similar business. When Mr. Kushner was asked in his deposition whether he had "any information from any source that Travis ever knew that there was a clause [in the agreement] about his parents not being allowed to engage in any similarly related business except through the company," Mr. Kushner replied that "Travis has testified that he didn't" and that he had no knowledge that the testimony was "true or not true." Accordingly, the defendant Travis Thompson is entitled to summary judgment on this issue.

With respect to the plaintiffs' contention that the defendant Travis Thompson conspired with the debtors to breach their fiduciary duty to the corporation, Lord George of Tri-Cities, Inc., by setting up a competing corporation, the court initially observes that any such cause of action belongs to Lord George, rather than the plaintiffs. *See NBD Bank, N.A. v. Fulner*, 109 F.3d 299, 300 (6th Cir. 1997)("[A]n action to redress injuries to a corporation cannot be maintained by a shareholder in his own name but must be brought in the name of the corporation."). Furthermore, even if such action were maintainable by the plaintiffs, the evidence presented to the

court does not establish a conspiracy to breach the debtors' fiduciary duty. According to the deposition testimonies, the defendant Travis Thompson set up the competing business in February 2001; the debtors left the Lord George corporation and turned the business over to the plaintiffs February 28, 2001, and began working for their son March 1, 2001.

As previously noted, the contractual prohibition on the debtors engaging in a business similarly related to Lord George expired upon the debtors' default in payment. And, under common law, although corporate officers have a fiduciary duty which prohibits them from engaging in a competing business to the detriment of their corporation, this duty ends upon the termination of office. *Venture Express, Inc. v. Zilly*, 973 S.W.2d 602, 604 (Tenn. App. 1998) ("Upon their resignation or termination, ... corporate officers generally are free to compete with their former corporation."). As recited in the *Zilly* decision:

> The fact that one was once a director or officer of a corporation does not preclude his engaging in a business similar to that conducted by the company. It is said that it is a common occurrence for corporate fiduciaries to resign and form a competing enterprise and that unless restricted by contract, this may be done with complete immunity, because freedom of employment and encouragement of competition generally dictate that such persons can leave their corporation at any time and go into a competing business.

Id.

Granted there was some indication in this case that the debtor Jill Thompson assisted Travis Thompson with some of the paperwork for the new business, i.e., the business' application for an employer number and Mrs. Thompson's employment application, in early February 2001, while the debtors were still with Lord George. However, mere preparations to compete do not constitute a breach of duty. *Id*. at 606 n.2 (officer's act of filing a corporate charter for new business not a breach of duty) (also citing *B & L Corp. v. Thomas & Thorngren, Inc.*, 917 S.W.2d 674, 679 (Tenn. App. 1995) (noting that corporate officer may prepare to compete prior to his termination from corporation); *Bancroft-Whitney Co. v. Glen*, 411 P.2d 921, 935 (1966)(mere fact that officer makes preparations to compete before he resigns his office is not sufficient to constitute breach of duty); *Parsons Mobile Prods., Inc. v. Remmert*, 531 P.2d 428, 432 (1975)(even before termination corporate director or officer is entitled to make arrangements to compete)). Because establishment of the competing business was not unlawful or accomplished by unlawful means, *see Birman Managed Care, Inc.*, 42 S.W.3d at 67 (definition of "conspiracy"); the defendant Travis Thompson is entitled to summary judgment on plaintiffs' claim that "the Defendants conspired with their son,

Travis Thompson, to set up a competing corporation."

The only remaining contention against Travis Thompson is that the debtors transferred to him Lord George assets, namely certain equipment, a van, and customer list. With respect to the equipment, Travis Thompson states in his deposition that he loaned Lord George the sum of $8,500 on his credit card and that the debtors partially repaid him by transferring to him certain cleaning equipment. Travis Thompson also states that at the time he had no knowledge that the equipment was subject to the plaintiffs' security interest, and that upon becoming aware of the security interest, he returned the equipment to the plaintiffs. The plaintiffs concede in their memorandum that the equipment has been returned.

Regarding the van, the debtor Craig Thompson testified that Lord George purchased the vehicle "a year or more ago" from Marco Machine Shop, that Marco retained a security interest in the vehicle to secure payment, and that thereafter Marco repossessed the vehicle. Travis Thompson testified that subsequently he purchased the van directly from Marco, and that he was still making payments to Marco. Because no evidence contradicted these statements, the court finds summary judgment in favor of the defendant Travis Thompson with respect to the plaintiffs' claim that the equipment and the van were

fraudulently transferred to Mr. Thompson.

The last item which the plaintiffs allege was fraudulently transferred was the Lord George customer list. The evidence does establish that the debtors gave this list to their son and that his corporation used it during the summer of 2001 to prepare a mail-out to potential customers, resulting in "just a few" calls back. Travis Thompson testified that no other use was made of the customer list and Mr. Kushner admitted in his deposition that the list has been returned to him. The difficulty with the plaintiffs' claim against Travis Thompson on this issue is that there is no evidence that the plaintiffs have suffered any damages as a result of his one-time use of the customer list. Mr. Kushner states in his deposition that he has not talked to any one on the list who told him specifically that had they not gotten the mailing they would have used Lord George for their services. Mr. Kushner also stated that he did not know at that point how to calculate his damages. Absent proof of such damages resulting from anything other than legitimate business competition, Travis Thompson's motion for summary judgment must be granted.

IV.

In accordance with the forgoing, an order will be entered granting defendant Travis Thompson summary judgment and dismissing him from this adversary proceeding.

ENTER:

BY THE COURT

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MARCIA PHILLIPS PARSONS
UNITED STATES BANKRUPTCY JUDGE